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MASTER OF MILITARY STUDIES

Defense Spending and Reform

SUBMITTED IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE DEGREE OF
MASTER OF MILITARY STUDIES

Major Matthew A Markham

AY 11-12

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Executive Summary

Title: Defense Spending and Reform

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Thesis: If the Department of Defense (DOD) is to maintain a military that the United States can afford it must change its culture of spending and incentivize fiscal restraint, while at the same addressing the ballooning costs associated with entitlements, the misuse of military personnel to fill inherently commercial activities, the increase in contractors, and the inefficiency of large organizations within the Department.

Discussion: Many believe that the growing National Debt is the United States' biggest threat. Washington's unsustainable spending continues to endanger an already weak economy, and is making the United States less secure. The DOD budget accounts for approximately 20 percent of all federal government spending and the largest portion of discretionary spending. As a result of efforts to fend off the looming financial crisis, the department will face significant budget cuts. DOD is traditionally called upon to protect the United States and its interests through military action, but soon it will be called upon to help through fiscal action as well.

Conclusion: To shape an affordable, modern military that meets the nation's security needs, the DOD must analyze its budget, incentivize the institution to change the culture of spending, carefully match capabilities to responsibilities, and revamp its policies.

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Preface

The experiences and knowledge I gained in writing this paper are invaluable. The subject hits close to home and prior to conducting my research, I must admit, I was ignorant as to the extent that military entitlements impact the Department of Defense's budgeting process. There are suggestions in this paper that have not been thoroughly vetted to determine their potential unintended effects and that could anger my community. To those who disagree with aspects of this piece, I would ask only that you keep an open mind about entitlement reforms and at the very least, acknowledge the need for a serious discussion on defense spending. I would like to thank Public Notice for providing me with a video copy of their panel "Spending and Defending". I would also like to thank my Faculty advisor for helping and encouraging me throughout this process. Most importantly I would like to thank my wife who has assisted me in my research and spent countless hours proofreading my work—including this preface.

Introduction

By the close of the third quarter for Fiscal Year 2011, the Bureau of Economic Analysis estimated the United States' gross domestic product (GDP) to be \$15.17 trillion; with the fourth quarter report still pending. In contrast, the United States' National Debt has reached \$15.23 trillion, and the White House is raising the debt ceiling in order to meet financial obligations. As the national unemployment rate hovers around 8.5 percent the government struggles to reduce growing debt, while improving the economy. President Obama stated, "We face an economic crisis that has made things worse. Millions of Americans are looking for work. Across our country, families are doing their best just to scrape by..."¹ The United States' debt is surpassing the GDP and continued government spending, in an attempt to stimulate the economy, has resulted in increased borrowing from China.

China, now the largest holder of American Treasury Securities,² is a global competitor at best and an enemy at worst. The Chinese economy, one of the largest in the world, grew by 9 percent in 2011. Many would argue that China's growth, at least in some instances, has been at America's expense. China disregards trade rules, violates intellectual property laws, infringes on patent laws, and manipulates its currency.³ China buys U.S. dollars on the open market, keeping its own currency undervalued relative to the US Dollar, thereby making Chinese products cheaper. In 2005, then-director of the Congressional Budget Office, Douglas Holtz-Eakin, said borrowing money from China does not endanger the American economy.⁴ Other economists agree with Holtz-Eakin, reasoning that because the United States is the largest export market for China, China would have no interest in destabilizing the American economy. At the same time, these economists agree that other countries owning U.S. debt creates a "situation that makes the U.S. more vulnerable to decisions of overseas governments and the decisions of overseas investors."⁵

To cope with financial crisis, according to President Obama, the U.S. must “live within [its] means while still making the investments we need to prosper.”⁶ The President, therefore, will attempt to make cuts that decrease the nation’s debt by \$4 trillion over the next decade. These cuts will require all government departments and agencies to evaluate their spending practices and reduce operating costs.

Since the Cold War, Republicans and security-focused Democrats in Congress and the White House have protected the defense budget, framing the debate politically so any proposed cuts appeared unpatriotic or, at the very least, detrimental to national security. Spending itself has now become a national security issue however, and the DOD’s budget accounted for more than half of all discretionary spending in 2010.⁷ With Washington debating the most appropriate places to cut the federal budget and the United States reducing its overseas commitments in Iraq and Afghanistan, the military is now at the center of cost-cutting discussions.

The DOD must be introspective, evaluating its spending practices and internally conducting the same tough debates occurring on Capitol Hill. While some of the solutions identified in this process will be apparent and painless, others will be much more complicated and divisive. Ultimately, to shape an affordable, modern military that meets the nation's security needs, the DOD must analyze its budget, incentivize the institution to change the culture of spending, carefully match capabilities to responsibilities, and revamp its policies. The following pages will explain the federal budgeting process for defense, detail the ways in which DOD spends money, assess defense budgetary issues and problems, and present solutions to create a more efficient and fiscally responsible military.

Federal Budgeting for Defense

The proposed federal budget for fiscal year (FY) 2010 was \$3.5 trillion, 23 percent of the GDP; that same year, the federal government collected \$2.2 trillion total receipts, resulting in a \$1.3 trillion deficit; 20 percent of the budget was spent on defense, 40 percent on entitlements, Social Security, Medicare, and Medicaid, 34 percent on other mandatory programs and discretionary spending, and 6 percent on interest (see Table 1). Though defense spending may appear small in comparison to Social Security, Medicare, and Medicaid, the United States' defense spending, accounts for 43 percent of defense spending worldwide—and this figure does not include defense-related spending occurring in agencies outside the DOD. The country with the second highest percentage of global military spending is China with 7 percent, and United Kingdom comes in a distant third with 4 percent (see Table 2).⁸

Table 1	
Adjusted Baseline Federal Budget by Category 2010	
(In Billions of Dollars)	
Outlays:	
Appropriated (discretionary) programs:	
Security	815
Non-security	491
Subtotal, appropriated programs	1306
Mandatory programs:	
Social Security	701
Medicare	446
Medicaid	273
Troubled Asset Relief Program (TARP)	-110
Other mandatory programs	644
Subtotal, mandatory programs	1954
Net interests	198
Total outlays	3,456
Receipts:	
Individual income taxes	899
Corporation income taxes	191
Social insurance and retirement receipts:	
Social Security payroll taxes	632
Medicare payroll tax	180
Unemployment insurance	45
Other retirement	8
Excise taxes	67
Estate and gift taxes	19
Customs duties	25

Deposits of earnings, Federal Reserve System	79
Other miscellaneous receipts	21
Total receipts	2,163
Deficit	1,292
Net interest	196
Primary deficit	1,097
Source: Derived from FY 2012 Budget from the Office of Management and Budget	

Table 2 Top 10 Military Spenders in 2010 (Spending in billion of U.S. Dollars)				
Rank	Country	Spending	Percent of GDP	Percent of World Spending
1	USA	698	4.8	43
2	China	[119]	[2.1]	7
3	United Kingdom	59.6	2.7	4
4	France	59.3	2.3	4
5	Russia	[58.7]	[4.0]	4
6	Japan	54.5	1.0	3
7	Saudi Arabia	45.2	10.4	3
8	Germany	[45.2]	[1.3]	3
9	India	41.3	2.7	3
10	Italy	[37]	[1.8]	2
	World	1630	2.6	
[] = estimated figure Sources: Stockholm International Peace Research Institute, <i>Background paper on SIPRI military expenditure data</i> Public Notice, "Spending and Defending				

Defense spending has become a highly debated and divisive issue as the U.S. faces a mounting fiscal crisis. With the U.S. out-spending the next closest country by more than six times, Admiral Mike Mullen, Chairman of the Joint Chiefs of Staff, is correct when he says, "The biggest threat to our national security is our debt."⁹

The Obama Administration realizes that this spending must be reduced and has outlined several plans to cut defense spending across the board. In September of 2011, the President laid out a ten-year plan to cut \$580 billion from mandatory programs, \$320 billion from federal health care programs, and achieve more than \$1 trillion in defense savings by drawing down forces in Iraq and Afghanistan.¹⁰ In January 2012, President Obama proposed \$487 billion in

defense cuts over the next 10 years. According to the President, even with these cuts the United States will maintain a defense budget larger than that of the next ten countries combined.

Evaluating the DOD budget in conjunction with the Federal Budget, former Secretary of Defense, Robert Gates asserted, “It is no secret that the United States faces a serious fiscal predicament that could turn into a crisis of credit, of confidence, of our position in the world if not addressed soon ... as a matter of simple arithmetic and political reality, the Department of Defense must at least be part of the solution.”¹¹

How DOD Spends Money

Understanding the complex way in which DOD distributes its budget is the first step towards implementing change and comprehending the impact budget cuts will have on U.S. national security. According to the Defense Business Board’s (DBB)¹² Analysis of DOD’s FY2010 budget, the base budget was \$530.7 billion, \$660.7 billion when including overseas contingency operations. DOD’s spending is categorized into five major areas: Research, Development, Test and Evaluation (RDT&E); Procurement; Operation and Maintenance (O&M); Military Personnel (MILPERS); and Military Construction (MILCON).¹³

DBB estimates that RDT&E expenditures for FY2010 were approximately \$80.1 billion. RDT&E appropriations finance contractors and government installations in the research, development, and testing of equipment and materials. Typically these funds are spent on developing new or improved capability, which includes the purchasing of weapons systems, equipment, computer software, components, and materials. The funds can also be spent to increase performance by modifying equipment or systems, such as software upgrades to

operating systems. Additionally, RDT&E funds are used for both investment and expense costs. Investment costs include facilities or testing equipment required to support developmental activities, while expense costs include things like employee salaries.¹⁴

In FY2010, Procurement accounted for \$104.8 billion of the budget. Procurement funds finance non-construction-related investment items, and cover costs necessary to deliver those items. Additionally, procurement appropriations fund the cost of modifying existing items. Procurement appropriations are normally available for obligation purposes for three years, except for the Shipbuilding and Conversion, Navy appropriation, which is available for five years.¹⁵

O&M funding, which grows at a rate of approximately 3 percent annually, was estimated to be \$184.5 billion for FY2010. O&M funding is categorized as appropriations spent on expenses rather than investments. O&M funds are closely associated with readiness. They are the commanders' primary source of funds for operating the force. O&M funds allow commanders to purchase fuel, spare parts, and equipment that fails to meet procurement thresholds (\$250,000), as well as pay for travel expenses, minor construction projects, training and education, and maintenance. O&M appropriations are not related to MILPERS or RDT&E, but can be used to finance civilian/contractor salaries not associated with RDT&E. With the explosion of contractors operating within DOD, it is difficult to determine the amount of O&M funding spent to finance their salaries.¹⁶

DBB puts the cost of MILPERS for FY2010 at \$135.0 billion. MILPERS are appropriations funding the salaries and other compensation for active, reserve, and retired military personnel. For active duty personnel these funds provide military pay, allowances, clothing, subsistence, permanent change of station moves, and health care. A large chunk of these funds, \$46.7 billion, not including health care costs, go towards military retirement pay.¹⁷

The last of the five categories is MILCON; it represents the smallest portion of the DOD budget, making up approximately \$21.0 billion in 2010. MILCON appropriations fund projects greater than \$750,000 such as bases, schools, missile storage facilities, maintenance facilities, medical/dental clinics, libraries, and military family housing.¹⁸

Budgetary Problems

The DBB revealed several significant, unsustainable trends and problem areas including: military entitlements, military personnel serving in commercial activities, military personnel serving in governmental activities that should be filled by DOD civilians, increased contractors, and new organizations with large staffs with insufficient controls.

Perhaps the most contentious and politically charged trend is military entitlements. In 2010 there were 1.9 million military members collecting retirement benefits, compared to the 1.4 million active duty members collecting pay and compensation. The overwhelming majority of retirees retired at 20 years of service, approximately 750,000 of the 1.9 million retired. An estimated 17 percent of new military members will retire from active duty after 20 years, 47 percent of new officers and 15 percent of new enlisted men. In the end, taxpayers compensate military service members for 60 years after just 20 years of actual service. Additionally, as retirees reach the age at which they qualify for Medicare/Medicaid they remain on the TRICARE for Life program, adding considerably to military health care costs.¹⁹

In addition to retirement and health care, there are several other entitlements requiring closer scrutiny. The first is Basic Allowance for Housing (BAH). BAH, a form of tax free pay, is designed to provide the service member with a housing allowance covering living costs based on

fair assessments of a particular duty station's private sector, rental-housing market. BAH rates also depend upon the service member's rank and dependent status. The service member qualifies for BAH if he/she is not residing in government quarters.²⁰

The purpose of BAH is to provide adequate housing to the service member and his family, but there is a wasteful discrepancy in its application for married service members. When a service member marries a civilian, the civilian is considered the service member's dependent, the member receives a slightly higher BAH to cover the housing needs of a married couple. When two service members are married however, each receives the non-married, no-dependent BAH.²¹

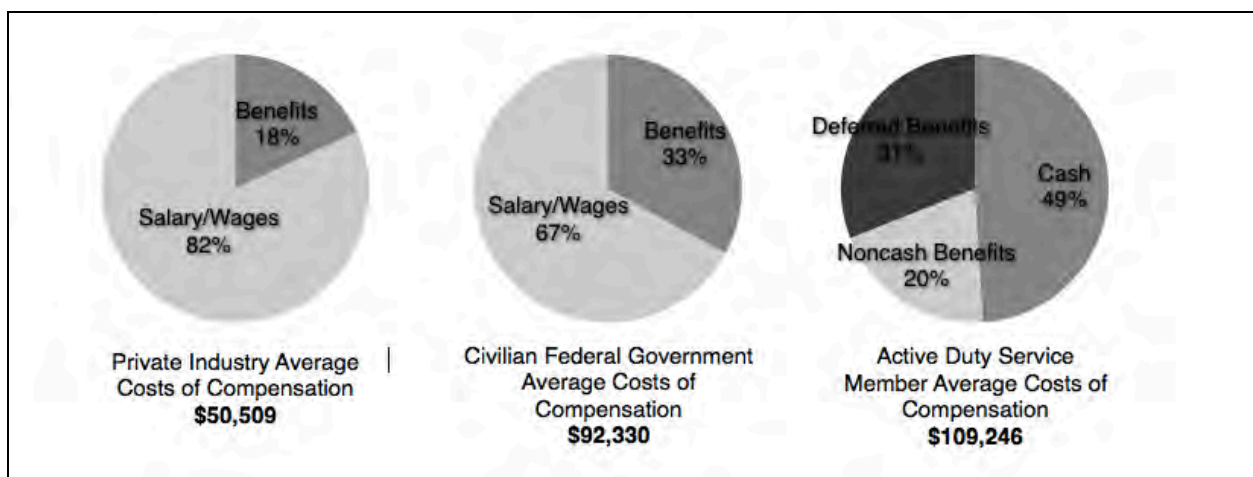
For example, the Washington, DC area BAH for a Major married to a civilian is \$3030. For a single Major, it is \$2592, thus if two Majors are married, each will receive \$2592. The first family is allotted \$3030 for adequate housing and the second \$5184, yet housing needs of both families are theoretically the same. Introduce a child into each family and the first family's BAH will not change as the spouse is already considered a dependent, while the second family's BAH increases to \$5622 to cover the new dependent, even though the housing needs of both families remain the same.²²

Basic allowance for subsistence (BAS) is another tax-free program. BAS, based on the USDA's food cost index, theoretically offsets the member's food costs. Unlike BAH, BAS does not take into consideration rank, location, or dependents; rates are fixed for enlisted and officers. The allowance covers only the cost of the service members' meals and not those of their families. BAS is rooted in the history of militaries providing members with room and board. The 2012 BAS rates are: \$348.44 for enlisted service members and \$239.96 for officers. Enlisted and officers must pay for any military-provided meals out of their BAS.

In the civilian world, salaried employees typically receive a bimonthly taxable paycheck

based on the local labor market and cost of living. From this sum, civilians pay for their housing, food, and all other expenses. The military is not unique in requiring housing and subsistence. Yet, service members receive tax-free pay to provide these. While BAH and BAS have specific functions in theory, in reality, they amount to a tax-free entitlement and should be treated as such in budget discussions.

In 2005 the U.S. Government Accountability Office (GAO) compared 2003 compensation costs between private industry, civil federal government, and active duty military. The below pie charts demonstrate that active duty compensation far exceeds private industry and civil federal government compensation. Between 2000 and 2004, active duty compensation increased significantly; basic pay grew by 23 percent, special and incentive pay by 30 percent, housing allowances by 66 percent, and health care costs by 69 percent. While military compensation exceeds all other sectors, 80 percent of military members believe that they receive less pay than their civilian counterparts.²³ In 2005, GAO recognized that growing deficits, rising health care costs, and comparatively low federal revenues make the current military compensation system unreasonable, inappropriate, unaffordable, and unsustainable.²⁴



Source: U.S. Government Accountability Office²⁵

The Post 9-11 G.I. Bill is another entitlement requiring reevaluation. The cost of this legislation is astronomical. Currently, a member who served a total of 90 days and received a honorable discharge after September 11, 2001, qualifies for the benefits regardless if they paid into the Montgomery G.I. Bill. In fact, even officers who were educated in the service academies, at taxpayer expense, are entitled to the benefits of the 9-11 G.I. Bill. Moreover, these benefits can be transferred to the military members' dependents if the service member has six years of active service. The annual maximum amount of tuition the bill covers \$17,500, but it will also provide up to \$1,000 annually for books and \$1,368 monthly for BAH while the beneficiary is enrolled in classes.²⁶ With over 1.4 million military members these costs will continue to grow with personnel turnovers.

As the deficit increases by approximately \$1 trillion per year and military entitlement costs grow exponentially, less of the DOD budget will be spent on actual defense. In a panel hosted by Public Notice entitled "Spending and Defending," Loren B. Thompson, Chief Operating Officer for the Lexington Institute and Chief Executive Officer of Source Associates, acknowledged the potential political suicide elected officials face when taking on military entitlements. Thompson suggests that because politicians are unwilling to jeopardize their political careers by cutting entitlements, the only way to truly reduce entitlement costs is to reduce the DOD's manpower.²⁷

In 2010, 40 percent of active duty members had never deployed. The DBB analyzed the way in which military members were performing non-military functions and what that meant in dollars. The Federal Activities Inventory Reform Act requires federal agencies to conduct a yearly inventory of what commercial activities are performed by federal employees. Commercial activities are services that can be performed by the private sector and are not so

intimately related to public interest as to mandate them as inherently governmental activities. Commercial activities would include gathering information, dispensing advice, providing certain types of security, administering the mail system, running the cafeteria, maintaining facilities, and managing the warehouse or motor vehicle fleet operations. According to the FAIR inventory of 2009, 339,142 uniformed military members performed commercial activities.²⁸ Comparing the compensation cost of Private Industry and Government Civilians to those of DOD personnel this is clearly not cost effective. Eliminating the 339,142 commercial positions performed by DOD personnel would save DOD \$37 billion annually.²⁹ By replacing those positions with private industry personnel, DOD would save \$20 billion annually and by replacing the positions with Federal Government Civilian employees, DOD would save \$6 billion annually.³⁰ The DBB estimates that today's average cost for DOD personnel is \$160,000, much higher than it was in 2005.³¹

When geared towards cutting costs, shifting commercial activities to the private sector can create significant savings. Reducing expenses however, has not been the driving force behind the post 9-11 explosion of contractors. The rapid expansion of government contracts over the past decade instead resulted from attempts by independent commands to fill personnel and capability gaps—real, imagined, and created. With relatively no control mechanisms, the burst of contractor positions has been inherently inefficient, often duplicating efforts, and extremely costly.

Analysis of the staffs at Combatant Commands (COCOM) in 2009 shows an estimated 10,800 contractors across the ten COCOMs. These numbers do not take into consideration contractors below the COCOM level. The actual number of contractors and their precise cost to DOD is hard to capture, as most contractors are paid with O&M funds, which makes

accountability difficult. According to estimates, in 2009 more contractors worked at Joint Forces Command (JFCOM) than military and government civilians.³² While, DOD has since disbanded JFCOM, which is structurally mirrored by Central Command (CENTCOM) and Transportation Command (TRANSCOM), it provides the perfect example of the exacerbation of the problem.

The final unsustainable trend highlighted by DBB is organizations with large staffs and insufficient controls to ensure efficiencies. Once again DBB uses the COCOMs to illustrate their point, estimating the number of personnel—military, civilian and contractors—at the 10 COCOMs combined to be 98,000, accounting for \$16.5 billion of the 2009 budget. In addition to COCOMs, Defense Agencies (DA) continue to grow and spend. In 2009 DA spent over 20 percent of the budget. DBB argues that the number and scope of DAs has exceeded current management and oversight mechanisms. In short, the services are being overcharged for DA activities.³³

There are over 15 trillion reasons why DOD should implement processes and reform policies to effect change and promote better spending practices. In addition to providing unsustainable trends the DBB has identified the barriers to spending changes perceived by senior DOD personnel. DOD personnel find that turf protection and the stove-pipe structure of the department makes it difficult to change the culture and institution. Senior leadership turns over rapidly and causes organizational misalignment in the eyes of personnel. The Chairman of the Joint Chief of Staff (CJCS) is appointed by the president and confirmed by the Senate for only a two-year term, after which he can potentially be reappointed for an additional two terms. Yet, because the CJCS serves “at the pleasure of the president,” and turnover at the White House occurs every four or eight years, it is rare for a CJCS to actually serve 3 consecutive terms. Similarly, the service chiefs serve four-year terms, often off cycle with the CJCS.

Entrenched politicians and civilian leadership make change difficult and DOD cannot overcome many of its budgetary issues without congressional action and civilian leadership intervention. Clearly, many budgetary issues are beyond DOD's scope but DOD can and must solve those problems that are within its control.

Proposed Solutions

The Federal deficit is a problem bigger than DOD and to solve it Washington must take a whole government approach. As Washington attempts to make cuts across the board and eliminate waste, DOD has a responsibility to do the same while maintaining its ability to provide for the external security to the United States and its interests. Service Chiefs have taken a hard look at their services' force structures and have made recommendations on downsizing the force in relation to threats and defense responsibilities. DOD has already dissolved JFCOM, who had more contractors on staff than military personnel. Both are important steps in saving on defense spending, but there is a long way to go. If DOD is to maintain a military that the United States can afford it must change its culture of spending and incentivize fiscal restraint, while at the same addressing the ballooning costs associated with entitlements, the misuse of military personnel to fill inherently commercial activities, the increase in contractors, and the inefficiency of large organizations within the Department.

The DOD's 2005 Base Closure and Realignment Commission (BRAC) is a prime example of a solutions model for defense spending cuts. Then SECDEF Donald Rumsfeld, defined the primary goal of BRAC as military transformation. "While acknowledging the importance of savings as a BRAC goal, the Commission went beyond a business model analysis of DOD's

recommendations and weighed the strategic environment within which recommendations would be implemented and their effect on DOD's transformational goals."³⁴ BRAC evaluated DOD's recommendations in the context of stabilizing or increasing force structure, with installations gaining missions and resources due to closures and realignments of other installations, saving money while maintaining capabilities. Though the total cost for 2005 BRAC exceeded \$35 billion the annual savings total \$4 billion; when combined with BRAC rounds of 1988, 1991, 1993, and 1995, the total annual savings jumps to \$12 billion. Over the next two decades, the 2005 BRAC is expected to save over \$40 billion.³⁵ The success of BRAC also demonstrates that political resistance to defense cuts in congress, while sizeable, is not insurmountable. Although legislators with an interest in preserving installations within their state or district fought fiercely against specific BRAC recommendations, ultimately, the Commission achieved its objective. A similar method could be used to address other politically charged defense spending issues such as entitlements and acquisitions.

Probably the most important, yet difficult, step is changing the culture of spending throughout the department. The current economy, increased fiscal deficit, and reduced tax receipts/revenues only highlight the importance of effectively managing limited resources. The DBB interviewed several senior DOD officials who spoke of the cultural barriers in obtaining lasting change and overwhelming resistance to change. DOD personnel feel that altering the culture of spending is difficult due to turf protection, unrealistic expectations, rapid turnover of senior leadership, and the misalignment of individuals involved in implementing solutions.

Former Deputy Secretary of Defense (DEPSECDEF) William Lynn stated, "The biggest challenge in instilling a culture of savings at the Department is changing the way people think. We need to change people's thinking so they think about the costs of things they're doing as well

as the value. It's the biggest challenge, but it's probably the most important endeavor.”³⁶ As implied, behavioral change is a long-term effort that requires continuous evaluation and improvements. The DBB provided four recommendations to the Secretary of Defense (SECDEF) to enable cultural change within his department.

The first step recommended by DBB is to commit the DEPSECDEF to a more intense role in leading a cultural change initiative. DEPSECDEF should consult with advisory boards to leverage expertise in developing business processes and changing management practices to produce a support structure that oversees a cultural transformation initiative and maintains the initiative's momentum once it is underway. The top tiers of leadership must be the driving forces behind changing a culture of spending. The recommendations of advisory boards and initiatives of top leadership cannot be empty rhetoric.

Secondly, SECDEF and DEPSECDEF must create a plan and process to launch a formal cultural change. Communication between DOD personnel is vital to explain the rationale, intent, and benefits behind the cultural change initiative, as well as risks of not being successful. Thirdly, DEPSECDEF must set achievable goals and define roles and responsibilities of leadership to build confidence and promote initiative buy-in. Leadership must be trained in managing desired changes. Lastly, in addition to training, leadership must be evaluated through metrics and rewarded for the implementation of change initiative. If implemented correctly DBB recommendations are designed to “promote risk taking, a willingness to change, a mindset of affordability with taxpayers' funds, continuous improvement, and preservation of funding levels that will support the Department's core mission to safeguard and defend the United States.”³⁷

In addition to applying the recommendations of the DBB, it is important to initiate incentives for DOD employees that will align personal interests with those of their service and the taxpayer. Charles Koch, the Chief Executive Officer (CEO) for Koch Industries, the second largest privately owned company in the world, attributes the success of Koch Industries to Market Based Management (MBM). Koch describes MBM as the “application of the Science of Human Action in an organization.”³⁸ Koch argues by applying the principles that lead to prosperity in society to an organization, be it business or government, the organization will obtain results. MBM is a holistic system that must be understood in order to be implemented correctly, but one of its main tenets is motivating an individual within the organization to act in the interest of themselves and the organization.

There are both financial and non-financial incentives that motivate individuals; the key of MBM is to apply the incentive to individual employee that best motivates him to maximize his value. Structuring incentives to bring about cost effectiveness within DOD without unintentionally causing adverse impacts will be challenging. Leaders need the ability to incentivize their employees individually and will have to take into consideration an individual’s placed value on financial and non-financial incentives, as well the individual’s time preference. Time preference refers to a desire to see an immediate or long-term benefit when receiving compensation. Time preference should be a critical element when looking at entitlements. To effectively incentivize a culture of savings, DOD must first adopt incentives that align individual and service interests, reinforcing “doing the right things for the right reasons.” Secondly, leaders should be able to incentivize individuals differently and reward cost-effective and productive behavior. Lastly, DOD needs to arm leaders with multiple tools with which to reward employees

both financially and non-financially. Incentives must be designed to attract, motivate, and retain quality service members.³⁹

DOD should provide commanders the ability to give raises bi-annually based on performance and their service evaluation system. This can be accomplished in a fashion that will both incentivize the deserving and save money for DOD. DOD can stop providing automatic raises every two years of service and provide the increase in pay only to those individuals that demonstrate value to their organization. Koch warns that organizations should avoid automatic raises, as they produce a destructive sense of entitlement. Tuition assistance is another program that needs to be controlled by commanders to incentivize the force. Currently service members that qualify for tuition are eligible for \$4,500 in assistance.⁴⁰ These benefits should be given only to individuals who earn it. Commanders should be able to invest in the service members who will provide the biggest return on the investment. Additionally, commanders should be provided with a set number of leave days a year that they can reward for desired performance and behavior. These leave days can either be used by the individual, with little cost to the government, or sold back to the government at the end of active service.

Commanders have several non-financial incentives to motivate the force, such as appealing to service member's sense of duty, pride, beliefs, and satisfaction, but the primary is through awards. Commanders must take care to award only the truly deserving; Koch warns that false praise undermines trust. A non-financial incentive that is primarily used only on reenlistments are special military schools such as Airborne School. Commanders should be given a quota of specialty schools to incentivize their employees.

Incentivizing the force to align personal interests to those of their service will increase the service members' productivity and create a more effective military. Successfully changing the

culture of spending and aligning the interests of members with their branches will create a sustainable change within the services.

As referenced earlier, military entitlements are a contentious subject and any recommendations need to be analyzed to determine their financial benefits, as well as their positive or negative effects. One suggestion to reducing retirement costs would be to stop paying military retirement to individuals that are currently fulltime federal employees. If individuals opt to continue serving the federal government after reaching military retirement, then that time should be credited towards the number of year of active service on their military retirement. Once individuals truly retire from federal service then they should be allowed to collect retirement. This will eliminate “double dipping” and reduce costs for the taxpayer.

The DBB proposes modernizing the military retirement system by instituting a contribution system. The system would be based on the existing Thrift Saving Plan (TSP), but with the government matching contributions to service members’ accounts. The plan would be payable at ages comparable to Social Security and the service member will be able to take out loans against the account to cover education and health care. Additionally, government contributions would account for combat and hardship tours. DBB asserts that the proposed system would be fair to individuals who do not wish to serve for twenty years, would reward longer service, and would create an effective force shaping tool. DBB recommends that the system be phased-in to ensure current military personnel are treated fairly with consideration given to costs. The DBB system is affordable and sustainable, but fairness is in the eye of the service member.⁴¹ Service members who reach the rate of E-6/O-4 or above, or 10 years of active service or more, should be given the option to remain on the old retirement plan or adopt the new plan.

Another entitlement/compensation program to evaluate and overhaul is BAH. BAH should be provided to service members only if adequate base housing is not available. Additionally, when service members marry other service members, DOD needs to discontinue the practice of providing housing allowances to both military members. The service member senior in rank should receive the BAH rate with dependents for his or her current grade. Both service members should receive BAH only when living in different geographical locations as a result of orders, and then they should receive the BAH rate for their current grade without dependents. If they have a child then the parent with senior rank should receive with dependent BAH rate. In the example provided this would save the DOD \$25,818 a year for one family. Though the overall savings for the military would be hard to calculate this would reduce MILPER costs and this is just one potential way to reduce housing costs for DOD.

BAS needs to be discontinued. If basic pay doesn't provide service members with enough money to purchase food, then raise basic pay. Service members E-5 and below that live in government quarters should be provided with meal cards that allow them to eat in base chow halls. Additionally, the military should discontinue the practice of charging for meals that service members eat during training or deployments. This would increase O&M costs, but would reduce MILPERS costs by half a billion dollars. Half a billion dollars might seem insignificant in comparison to the DOD budget, but to change the culture of spending nothing can be viewed as insignificant. If BAS is continued as is, per diem rates paid to service members during temporary assigned duty should all be reduced by eight dollars, the equivalent of 1/30 of the current officer BAS.

The 9-11 G.I. bill needs to be totally restructured. First, there must be a financial buy-in from service members to help fund the program, with waivers available for individuals who did

not buy in but are unable to continue on active duty due to injury. Secondly, the transferring of benefits should be limited to instances where service members are incapable of providing for their families due to death or injury. If education benefits for service members' families are to be an incentive for recruitment or retention, then DOD should establish a college savings plan for military members' families.

Military members who are performing commercial activities are a poor use of DOD resources. As discussed earlier, DOD employees are generally much more expensive than private industry or government civilians. With estimates for the average military personnel costing DOD \$160,000, DOD needs to eliminate these activities. If DOD can cut just 10 percent of these positions it would save \$5.4 billion annually.⁴² An independent auditor should evaluate these positions to determine which can be eliminated completely and which can be transitioned to either private industry or a government civilian employee.

Reducing contractors, limiting the growth of organizations, and ensuring controls are in place to establish efficiency are closely related. First, it is necessary to cap the size of organizations and the number of contractors working in them at their current levels. Secondly, an independent auditor must evaluate all organizations to reduce duplication and overlap. Thirdly, DOD must implement processes for tracking and controlling the number and cost of personnel in each organization, preventing costs from being lost in O&M funding. Lastly, DOD must make organizations, especially DA, more cost effective by adopting best business management practices, consolidating overhead functions across organizations, and eliminating, privatizing, and merging positions.⁴³

Conclusion

The federal deficit surpasses the GDP and continues to grow. The United States cannot maintain a strong military with a weak economy; something must be done. The drawdown of military forces in Iraq and Afghanistan raises the question: does the United States need to vastly outspend the rest of world in order to maintain its security? Washington is already looking towards the military's budget as a place to cut spending. It is the responsibility of DOD to properly restructure the force and reduce costs so as to fully meet the nation's security threats as well as budget constraints. DOD will have to make unpopular decisions, change its culture of spending, and end the sense of entitlement as it overhauls unsustainable practices and bad policies. Not all cost saving ideas are going to be good ones and some that appear to be good will have unintended consequences, but all ideas must be seriously considered and scrutinized. Congress and DOD civilian leadership must work closely with senior military leaders to achieve DOD finance reform. Taking these steps will reduce DOD spending while maintaining military superiority.

Endnotes

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